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2 UNITED STATES BANKRUPTCY COURT

3 SOUTHERN DISTRICT OF NEW YORK

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5 In the Matter

6 of

Case No.

01 B 14312

7 MAGNESIUM CORPORATION  
8 OF AMERICA,

8

Debtors.

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10

February 14, 2003

11

United States Custom House

12

One Bowling Green

New York, New York 10004

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14 Motion of Ad Hoc Committee for the  
15 Appointment of a Trustee or Alternatively  
16 Conversion of this Case to Chapter 7.

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B E F O R E:

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HON. ROBERT E. GERBER,

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U.S. Bankruptcy Judge.

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FILED  
FEB 24 11:54  
U.S. BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK

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2 A P P E A R A N C E S (Continued):

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MARK ELMER, ESQ.

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1 Magnesium Corporation of America

2 P R O C E E D I N G S

3 THE COURT: Good morning, please be  
4 seated. Okay, Magnesium Corporation of America.

5 Can I get everybody who wants to be  
6 heard on that one up at the counsel tables, please?  
7 I gather there may be some people on the phone. I  
8 want everybody to identify themselves on the record  
9 both in the courtroom and then on the phone. And I  
10 want you to sit down, I have some comments I want  
11 to say.

12 For the Debtor I see Mr. Smolinsky;  
13 for the movants, Ms. Grubin; and Ms. Davis for the  
14 U.S. Trustee.

15 Are you also here to appear for the  
16 U.S. Trustee?

17 MR. CHANG: Yes, although I'm here  
18 to observe only.

19 THE COURT: Anybody else in the  
20 courtroom?

21 MR. SMOLINSKY: Your Honor, I would  
22 ask if your Honor is agreeable to find out who is  
23 in the courtroom today, even if they are not  
24 planning on speaking and to find out which parties  
25 they represent.

1 Magnesium Corporation of America

2 THE COURT: Is there anybody here  
3 who is a counsel for another party who is in the  
4 courtroom? I don't think it's appropriate for me,  
5 Mr. Smolinsky, to ask if anybody is in the press or  
6 anything who is observing the proceeding.

7 Who is on the phone?

8 MR. TOP: Your Honor, Frank Top from  
9 Chapman & Cutler on behalf of the official  
10 committee.

11 THE COURT: Good morning.

12 MR. TOP: Good morning to you.

13 MS. WALLACE: Marianne Wallace from  
14 Shipman & Goodwin on behalf of the Indentured  
15 Trustee, U.S. Bank National Association.

16 THE COURT: Yes, I read your  
17 signature.

18 Anyone else? Okay, fair enough.

19 As is usual in my Court, when it's  
20 time to make your presentations, I want you to make  
21 them as you see fit. But I had problems with both  
22 sides' briefs that were submitted on this motion of  
23 a failure to drill down as to what I see as the  
24 real issues on this.

25 Some of my comments are obviously

1                   Magnesium Corporation of America  
2   going to be directed toward the movants, others,  
3   roughly an equivalent number, are going to be  
4   directed toward the debtor.

5                   My general view is that where  
6   there's no debtor misconduct or incompetence, and  
7   we haven't had any indications of that here,  
8   although obviously I'm aware of the conflicts in  
9   this case of interest that have been alleged by the  
10   movant, that you get the most money into the  
11   pockets of creditors by keeping or preserving the  
12   benefits of the debtor in possession and the debtor  
13   in possession's counsel. And dealing with conflict  
14   type issues by the issuance of an STN or Commodore,  
15   Housecraft type of order.

16                  The issue in this case is whether a  
17   Commodore, Housecraft, STN type order is going to  
18   skin the cat or not or whether the interests, the  
19   needs of the creditors, require more than that.

20                  I was puzzled by the fact that  
21   neither side in its brief addresses what I think is  
22   key; and although it appeared in nobody's brief, it  
23   appeared in a letter that was attached to the  
24   movant's reply.

25                  The creditors may want to make a 108

1                   Magnesium Corporation of America  
2   argument for the next couple of years, reach back  
3   and bring on any kinds of avoidance actions, which  
4   when you are talking about events that took place  
5   in 1996, might be significant, at least if, and to  
6   the extent, that New York statutes of limitations  
7   apply, which normally don't go beyond six years,  
8   except in the case of fraud length concealment.

9                   I was really, really surprised that  
10   Ms. Grubin -- that the bondholders cited  
11   Cybergenics for a host of reasons, not just that  
12   it's vacated, not just that it's been so widely  
13   criticized by just about everybody, other than the  
14   panel of the three judges in the Third Circuit who  
15   issued that decision, but most fundamentally,  
16   because we are in the Second Circuit where STN,  
17   Commodore and Housecraft are the controlling  
18   authority on me.

19                   I have zero doubt that I can vest in  
20   the Creditors Committee, the power to fully  
21   prosecute the kinds of actions that we are talking  
22   about. And I have almost as much certainty that I  
23   can authorize the bondholders to do it as well.

24                   So the issue in my mind is whether,  
25   with that power, it's better for creditors to give

1                   Magnesium Corporation of America  
2    them the STN, Commodore authority, on the one hand,  
3    or to additionally appoint a Trustee. And I was  
4    surprised and a little disappointed that the  
5    movant's papers didn't address what I think may be  
6    the things that we're going to be hearing from Mr.  
7    Smolinsky, as to the interest of creditors is  
8    better served in doing battle with PacificCorp and  
9    dealing with the needs and the concerns of the EPA  
10   to keep incumbent counsel or management in place  
11   where they have issues.

12                   Mr. Chang's letter underscored that,  
13   which if accepted by the Utah courts or the Utah  
14   PSC or by entities other than me, could give rise  
15   to very substantial administrative costs, that  
16   would ensure that nothing is left for the  
17   unsecureds.

18                   I also do not believe that in any  
19   way, shape or form this case is a Hampton Hotel  
20   case.

21                   Now, with that said, Mr. Smolinsky,  
22   you acknowledge, as you must, that at least an STN  
23   order is appropriate here. But I have some  
24   difficulty in seeing how I can deprive the  
25   bondholders the ability to argue the 108 point, if



1                   Magnesium Corporation of America

2    any, that they can squeeze out a little extra time  
3    on the statute of limitations on the 108 or if they  
4    want to try to make an argument of that character.

5                   I haven't focused on the 108 point  
6    in several years. And the last time that I focused  
7    on it, and I recognized that my learning on this is  
8    very stale, I recall then that the applicability of  
9    108 was a matter of debate and that there was a  
10   conflict in the cases on that point.

11                  It seems to me that is one of, at  
12   most, two ways of getting money into the pocket of  
13   the estate, and therefore, into the pockets of the  
14   creditors, I have difficulty seeing how I can  
15   deprive the creditors to have the opportunity to  
16   make their 108 argument without prejudging how I  
17   would decide the 108 actions once they were made.

18                  So, if that is the case, that tilts  
19   in favor of me appointing a Trustee of one type or  
20   another under 1107, even though in the perfect  
21   world, I would like to keep the incumbency we're  
22   dealing with to the PacificCorp issues, and to the  
23   extent relevant or appropriate, the EPA issues.

24                  The second point that you make,  
25   which is that there is potential money on the

1                   Magnesium Corporation of America  
2   table, but only if the outcome of this hearing is  
3   favorable, in what I think was articulated in one  
4   or another of the papers as the sole discretion of  
5   one of the other -- of the debtor's affiliates,  
6   strikes me as heavy-handed. Saying that there  
7   might be some kind of money to throw in the pot to  
8   meet administrative expenses if somebody is pleased  
9   with the outcome of this hearing is, and I don't  
10  think it's just a matter of my ego, offensive to  
11  me. It's not a bribe, of course, at least it's not  
12  a bribe of me, but why in a thousand years should I  
13  let a veiled threat like that one influence the way  
14  I decide things today.

15                   The only issue, as far as I'm  
16  concerned -- and I think you can see why I was  
17  troubled by the failure of the papers to really get  
18  their arms around this issue -- is what's going to  
19  put more money into the pockets of creditors,  
20  administrative creditors and, perhaps  
21  unrealistically, unsecured creditors by the amalgam  
22  of reducing administrative claims against the  
23  estate and by any accretion into the estate that  
24  might occur as a consequence of litigation against  
25  a third party, which might ultimately turn out to

1                   Magnesium Corporation of America  
2   be successful, and that's what I need both sides to  
3   focus on in their arguments.

4                   I also did not see, and it may be  
5   because nothing was filed or it may be because  
6   something got lost out of my statement, of views  
7   from the U.S. Trustee; but, Ms. Davis, if you have  
8   any views, I would be very interested in hearing  
9   what views you have.

10                  MS. DAVIS:   Thank you, your Honor.

11                  THE COURT:   Ms. Grubin, I would like  
12   you to start up, and come up to the main podium so  
13   everybody can hear.

14                  MS. GRUBIN:   Very good, your Honor.  
15   Your Honor, Janice Grubin here from Golenbock,  
16   Eiseman, Assor, Belle & Peskoe. And as the court  
17   knows, we are co-counsel and we are here on behalf  
18   of the Ad Hoc Committee of senior noteholders. And  
19   it is our motion for the appointment of a Trustee  
20   in the Chapter 11 here in these cases, or  
21   alternatively, the conversion of this case to a  
22   Chapter 7. I have in the courtroom two  
23   representatives of this committee. The AIG  
24   Investment Corp., as well as Ramius Capital Corp.  
25   and I might say one of those two persons has to

1                   Magnesium Corporation of America

2    leave a little earlier, and I apologize for any  
3    disruption that will cause.

4                   Your Honor, I will obviously direct  
5    my argument to the court's concerns and dispense  
6    with laying the foundation that I was prepared to  
7    argue this morning and will simply incorporate by  
8    reference, all of the arguments and statements and  
9    representations made in both our motion as well as  
10   in our reply that was filed and served yesterday.  
11   We would incorporate obviously by reference all of  
12   the arguments made.

13                  I would also note, your Honor, this  
14   is not a contested hearing. There are no facts  
15   that appear to be at issue, and this is appearing  
16   to be a legal argument here. And we believe we  
17   have met all the facts on the legal cause under  
18   1104 as well as 1112(b).

19                  With respect to our view as to what  
20   will put the most money, cutting right to the  
21   chase, what will put the most money in the pockets  
22   of the creditors here, not surprisingly, your  
23   Honor, it is our view that either a Chapter 11  
24   Trustee or a Chapter 7 conversion will generate --  
25   it has the potential to generate more recovery for

1                   Magnesium Corporation of America  
2   all creditors than if the case remains in the  
3   Chapter 11 without a Trustee and continues its  
4   winddown, presumably by some kind of a liquidating  
5   plan.

6                   We believe that the estates are  
7   administratively insolvent, although the debtor has  
8   not quite conceded to that, and you know, there  
9   really is -- debtor's counsel has admitted that it  
10   has about 300,000 dollars in unpaid fees. The most  
11   recent operating report indicated 245,000 dollars  
12   in cash and cash equivalents.

13                   THE COURT: In the till you mean?

14                   MS. GRUBIN: Excuse me. 245,000  
15   bucks in the till, yes, as of October 31, 2002.  
16   And paragraph 11 of the debtor's objection  
17   indicates that they have unpaid fees of  
18   approximately 300,000 dollars.

19                   THE COURT: All to Chadbourne or are  
20   there other folks who haven't been paid either?

21                   MS. GRUBIN: I believe it was only  
22   to Chadbourne that was represented.

23                   THE COURT: Okay.

24                   MS. GRUBIN: And, you know, frankly,  
25   your Honor, we don't understand how it is that the

1                   Magnesium Corporation of America  
2   debtor will be able to continue to fund this  
3   litigation or whatever it needs to do with  
4   PacificCorp or anything else in the case, absent  
5   this proposed funding by the debtor's affiliate,  
6   which seems to us to be very vague and oblique, and  
7   we really don't understand the terms of that  
8   funding. It seems very unilateral.

9                   We understand it may be presented to  
10   the Court for approval, but we think it is another  
11   evidence of control in this case by affiliated  
12   parties, and including Mr. Rennert, and we don't  
13   think it's appropriate.

14                  For these reasons, we believe it is  
15   appropriate for this Court to appoint a Trustee, or  
16   perhaps convert this case. It's in its discretion  
17   the court can do that, the court knows that, and  
18   get a Trustee on board who is aware of the risks in  
19   this case and can bring in counsel who can conduct  
20   the kind of investigation and possibly litigation  
21   that the committee began so many months ago.

22                  We really believe -- I know that my  
23   clients have conferred with a number of counsel on  
24   a variety of issues, including the statute of  
25   limitations issues under 108(a), and they have

1                   Magnesium Corporation of America

2     concluded, particularly the law firms whose papers  
3     we have attached to our reply, that there are  
4     viable causes of actions here that they are  
5     prepared, after a brief investigation, to  
6     prosecute.

7                   And this is an experienced firm that  
8     does a lot of contingency work in bankruptcy. They  
9     spent 60 to 80 hours reviewing the various files in  
10    this case, and it is their considered opinion that  
11    there are viable causes of action here. And they  
12    have asked and are concerned about the fact that  
13    while we are in the Second Circuit, and, your  
14    Honor, the trilogy of decisions, STN, Commodore and  
15    Housecraft, indicate that this Court has the  
16    ability to approve an agreement between counsel and  
17    -- the debtors and the creditors authorizing such  
18    creditors either in the capacity of a committee or  
19    sole creditors such as, for instance, this  
20    bondholder committee to prosecute avoidance causes  
21    of action. There is still some uncertainty if down  
22    the road Cybergenics has been vacated, but the  
23    hearing on that will be reheard this month, I  
24    believe.

25                   THE COURT: What difference would

1 Magnesium Corporation of America

2 that make, Ms. Grubin --

3 MS. GRUBIN: The difference --

4 THE COURT: -- for a bankruptcy

5 judge who considers the Second Circuit binding upon  
6 him.

7 MS. GRUBIN: If the Third Circuit  
8 issued its ruling whichever way, it's clear to me  
9 that it would be appealed. And if the Supreme  
10 Court granted cert and then it heard argument and  
11 issued an opinion, if that opinion embraced a  
12 position that was contrary to the established  
13 practice in this district --

14 THE COURT: This circuit?

15 MS. GRUBIN: Excuse me, your Honor,  
16 yes, in this circuit.

17 THE COURT: And every circuit other  
18 than the Third, insofar as I'm aware.

19 MS. GRUBIN: Yes, your Honor, that's  
20 correct. But because of that uncertainty, we are  
21 here before you to argue for the assignment of a  
22 Trustee under 1103 -- or 1104.

23 Truthfully, we have had  
24 conversations with Mr. Smolinsky under an STN like  
25 the Commodore, Housecraft stipulation, but we just



1                   Magnesium Corporation of America

2       couldn't get there. My clients could not.

3                   THE COURT: Well, the sticking point  
4       is you need 108 to bootstrap, don't you?

5                   MS. GRUBIN: Yes, we do. And we are  
6       also concerned under 546(a), that the two-year  
7       period is going to run out this August.

8                   And again, your Honor, I am not as  
9       close to the analysis of these claims because I was  
10      brought in as bankruptcy counsel to argue this  
11      motion and to draft this motion, but -- and I've  
12      been told the contemplated investigation is not  
13      going to be extensive to determine whether or not,  
14      finally, there should be prosecution of these  
15      claims avoidance actions under 546(a) that time  
16      period runs August -- August 27th, so we are  
17      concerned about that.

18                  THE COURT: Talk about their point  
19      concerning the benefits of the learning curve in  
20      dealing with issues raised by PacificCorp and by  
21      the EPA.

22                  MS. GRUBIN: Admittedly, there is a  
23      learning curve that's going to have to be utilized  
24      by a Chapter 11 Trustee or a Chapter 7 Trustee and  
25      that's -- perhaps that's why a Chapter 7 would have

1                   Magnesium Corporation of America  
2   to be utilized here because then you won't have to  
3   have a plan process to be conducted and you would  
4   have no need for a committee and you would  
5   automatically eliminate a whole host of  
6   professionals. I am confident that counsel can be  
7   appointed just as efficiently as Mr. Smolinsky's  
8   firm is.

9                   THE COURT: Would a Chapter 7  
10   Trustee or, for that matter, a Chapter 11 Trustee,  
11   be able to use Mr. Smolinsky as counsel for special  
12   purposes to deal with that?

13                  MS. GRUBIN: I think it would be  
14   considered if it was.

15                  THE COURT: Don't the talk quite so  
16   much as considered. Are you aware of any legal  
17   impediment to that? Yes or no.

18                  MS. GRUBIN: I am not.

19                  THE COURT: Continue, please.

20                  MS. GRUBIN: Your Honor, as the  
21   court knows, there is an overwhelming majority of  
22   creditors who joined in this motion and we have see  
23   motions in support of this, as well as the debtor  
24   and the trustee, and both of them are on the phone,  
25   and the only motion that's objected to is the

1                   Magnesium Corporation of America  
2    debtors. I submit that we have submitted the  
3    standards of cause under 1104 as well as under  
4    1112(b), and the only issues really is under that  
5    section. We will ask the court to grant the  
6    appointment of a Trustee here.

7                   We would point the court to the  
8    authority cited in our motion, particularly the  
9    Intercad case, the PSR Insurance case, the Corville  
10   William Vaughn and L.S. Good cases, which all of  
11   them acknowledge there are potentially causes of  
12   interest that constitutes cause alone under 1104,  
13   (2), and possibly (1), cause the appointment of a  
14   Trustee.

15                  THE COURT: I'll hear the (a) (2)  
16   argument. I have yet to hear anything that leads  
17   me to -- there is cause under (a) (1). I can see  
18   why you do believe -- I don't want to under  
19   strength the point of the issue, and vis-a-vis the  
20   conflicts case, makes it in the interest of  
21   creditors to appoint it, but I have to find a lot  
22   more under fraud or mismanagement. I need to see a  
23   lot more.

24                  MS. GRUBIN: Under 1102, we believe  
25   the conflicts situation has been created by what we

1                   Magnesium Corporation of America  
2   understand to be the kind of salient presence of  
3   Mr. Rennert and his affiliates throughout these  
4   cases to constitute cause under 1104(a)(2), such as  
5   it would be in the best interest of the creditors,  
6   in this case or in the interest of creditors that a  
7   Trustee be appointed and that the court appoint a  
8   Trustee.

9                   We don't think that the interest of  
10   equity should be considered because we believe that  
11   they have no stake left in these cases since the  
12   cases are administratively insolvent and I would  
13   submit to you, your Honor, that it's in the  
14   McCorville Publishing case and that's a Southern  
15   District case, where there are interests and the  
16   principles occupy conflicting positions in the  
17   transferee positions, a trustee should be appointed  
18   in order to investigate the financial affairs of  
19   the company and it certainly will warrant cause,  
20   which we also talk about in our case, that on the  
21   basis of a failure for the avoidance of a transfer  
22   to the tread, and the S.L.S. Good case talks about  
23   a specific, very wig good the action is all  
24   unsecured had can hope to realize. Which is really  
25   the situation here.

1 Magnesium Corporation of America

2 In all candor, there is nothing for  
3 the unsecured unless and until there is an  
4 appointment of some kind of recovery in avoidance  
5 and other causes of action, and we understand the  
6 committee began an investigation on the claims and  
7 causes of action. It was preliminary, and they  
8 were focused on officially trying to bring a non  
9 affiliated buyer to the table which would  
10 ultimately bring funds to the creditor; and there  
11 was a sale to U.S. Mag in June, which closed the  
12 end of June, and the case has been fairly  
13 relatively quiet since then.

14 And now it's eighteen months after  
15 the filing, your Honor, and we would say that there  
16 needs to be, in the best interest of the creditors,  
17 under 1104(a)(2), that a trustee needs to be  
18 appointed to complete the investigation that the  
19 committee began and determine once and for all  
20 whether there are viable claims here to prosecute  
21 those claims and see where that goes.

22 THE COURT: Okay, Mr. Top, if you  
23 have anything substantive to add to what Ms. Grubin  
24 has said.

25 MR. TOP: Thank you, your Honor. I

1                   Magnesium Corporation of America  
2    just want, again, to support Ms. Grubin's efforts  
3    and the efforts of the Ad Hoc Committee and just  
4    reiterate what she said. You know, when we came on  
5    board, frankly, after the bankruptcy was filed in  
6    late November, early December, we were kind of  
7    thrown into a position where the primary bulk of  
8    our time and efforts were spent on trying to find  
9    different alternatives to deliver value for  
10   unsecured creditors. Unfortunately, that did not  
11   bear any fruit.

12                   We did take a preliminary look at a  
13   number of avoidance actions, and obviously we have  
14   been able to give our financial advisers  
15   information about detailed insurance transfers that  
16   were made, and frankly, under state law type of  
17   avoidance action, we wouldn't have any presumption  
18   of solvency or anything of that nature.

19                   So while we have provided the Ad Hoc  
20   Committee with a list of certain transfers that  
21   were made that, frankly, I think even the debtors  
22   would admit to having occurred, there needs to be  
23   some investigation as to whether other elements of  
24   various state law type avoidance actions and the  
25   statutes request can be met, particularly as it

1                   Magnesium Corporation of America

2   relates to the solvency and the like.

3                   And, you know, unfortunately the  
4   debtor for this case asserts it would be very hard  
5   for the committee to engage a professional to  
6   undertake a lot of the investigation that would  
7   need to take place before we would feel comfortable  
8   filing a complaint ourselves, and that the  
9   resolution has been to try to find someone to do a  
10   lot of this work on a contingency basis, and the  
11   committee is supportive of allowing that to take  
12   place.

13                  THE COURT:   Okay, thank you.   Ms.  
14   Wallace, do you want to add anything?

15                  MS. WALLACE:   Your Honor, no, I have  
16   nothing to add to what's been stated by the  
17   previous two counsel.

18                  THE COURT:   Okay.   Before Mr.  
19   Smolinsky gets to speak, I want to give Ms. Davis a  
20   chance to give me her views and I want to give Mr.  
21   Chang another opportunity to speak if he wants to.

22                  MS. DAVIS:    Your Honor, while your  
23   Honor has an order in which you want to hear from  
24   the parties, I would very much appreciate hearing  
25   from debtor's counsel before I have an opportunity

1 Magnesium Corporation of America

2 to express my view. I think my comments will be a  
3 little more contributory if I hear from him first.

4 THE COURT: That's agreeable to me.  
5 Fair enough. Mr. Chang, I don't know if you want  
6 to speak now or not.

7 MR. CHANG: Very briefly, your  
8 Honor.

9 THE COURT: Sure.

10 MR. CHANG: I simply wanted to  
11 address one of the issues raised by the court,  
12 which, unfortunately, I didn't pick up in the  
13 papers. But the issue -- I'm not as prepared as I  
14 might be, but the issue is if the appointment of an  
15 trustee might ramble up on the litigations.

16 THE COURT: Well, maybe that's  
17 another way of saying it. You have a plenary  
18 litigation, your EMA client has plenary litigation  
19 pending out in Utah which I will not be the  
20 decision-maker on. But if your client is  
21 successful, you are going to have a whopping admin  
22 claim, as I think you stated in your letter.

23 Now, in some sense you've got a  
24 different perspective, and a kind of conflict with  
25 the other creditors, because if you are successful,



1                   Magnesium Corporation of America  
2    you are going to take money out of the bondholders  
3    pockets, which may be what federal law says is the  
4    appropriate result, and I take no view on that.

5                   But if I'm going to look at  
6    everybody's interest, other than the EPA's,  
7    obviously they have an interest in your client  
8    being unsuccessful, so that whatever scarce  
9    resources, or maybe not so scarce resources, go to  
10   their pockets, rather than the Federal Government's  
11   pockets, which is not an uncommon situation, but I  
12   would like to get your views. But I've also got to  
13   tell you that I look at it in that context.

14                  MR. CHANG: I understand, your  
15   Honor. I wasn't actually intending -- I think the  
16   Government's position on the trustee is, as we  
17   stated, we are taking no position. The only reason  
18   I came to speak is because I thought I understood  
19   the court to have a concern that putting a trustee  
20   in position at this point, because of the ongoing  
21   EPA litigation, might cause difficulties,  
22   because --

23                  THE COURT: Well, that's the  
24   debtor's contention, that's right.

25                  MR. CHANG: And that's the reason

1 Magnesium Corporation of America

2 I'm coming up to speak. To my knowledge, the EPA  
3 litigation is not being handled directly by  
4 Chadbourne and Parke. It's being handled by the  
5 law firm of Parsons and Bailey, and I don't know  
6 anything about the litigation. I don't know  
7 anything about PacificCorp, but it seems to me the  
8 appointment of the trustee wouldn't necessarily  
9 require if trustee to come up on -- all the way up  
10 to speed on the EPA action if it's simply  
11 transferring it over to Parsons and Bailey. It  
12 wouldn't cause that much destruction, unless Mr.  
13 Smolinsky can tell me what role Chadbourne & Parke  
14 played in the litigation.

15 THE COURT: Thank you, that's  
16 helpful.

17 MR. CHANG: Thank you.

18 THE COURT: Okay, Mr. Smolinsky.

19 MR. SMOLINSKY: Thank you, your  
20 Honor. Before I give my comments on the motion,  
21 I'd like to provide your Honor with a very brief  
22 status of the case. We have been undertaking to  
23 wind down the affairs until we received this  
24 motion. Obviously, we did not foresee an intensive  
25 litigation proceeding. So in that light, we have

1                   Magnesium Corporation of America  
2     filed for an administrative bar date. I believe  
3     the administrative bar date is actually today.  
4     And, obviously, we were intending on reviewing  
5     those claims and identifying how we would proceed  
6     toward disbursing other remaining funds in the  
7     estate.

8                   THE COURT: Mr. Smolinsky, what kind  
9     of admin claims did we have, other than those in  
10    the way of the 300,000 bucks or the stated 300,000  
11    bucks owing to your firm from whatever the EPA can  
12    recover?

13                  MR. SMOLINSKY: We have other  
14    professional claims. If your Honor would recall,  
15    we had agreed at the hearing back in, I'll say,  
16    November, with respect to the professionals  
17    receiving 70 percent of their fees, to allow a bar  
18    date to be filed so we could assess what the other  
19    claims are. So all of the professionals, I  
20    believe, have claims outstanding.

21                  THE COURT: Not just your firm?

22                  MR. SMOLINSKY: Correct.

23                  Chapman & Cutler, Peter Solomon on  
24    behalf of the committee as financial advisers. I  
25    think, besides my firm, Chapman & Cutler and Peter

1 Magnesium Corporation of America

2 Solomon have the largest claims.

3 THE COURT: What kind of order of  
4 magnitude are we talking about here?

5 MR. SMOLINSKY: I don't have that  
6 information with me. Perhaps Mr. Top would have  
7 that figure.

8 THE COURT: Okay, I don't want you  
9 to interrupt yourself, but, Mr. Top, make a note to  
10 see if you can fill that in when it's your turn.

11 MR. TOP: Say that again, your  
12 Honor, how much we are outstanding?

13 THE COURT: Yes.

14 MR. TOP: Less than 100,000 dollars,  
15 I believe it's like between 50 and 75,000 dollars.

16 MR. SMOLINSKY: I think the Peter J.  
17 Solomon piece was larger than the Chapman & Cutler.  
18 I don't recall if it was 150 or slightly more than  
19 that.

20 THE COURT: Okay, thank you.

21 Go on, Mr. Smolinsky.

22 MR. SMOLINSKY: In addition, there  
23 are reclamation claims in over the course of the  
24 last couple of months, we have been in conversation  
25 with the reclamation creditors over the amount of

1                   Magnesium Corporation of America  
2    their claims. I actually have one or two  
3    stipulations that I've been pressured over the last  
4    couple of weeks to file, but I've chosen not to  
5    because of this motion. I didn't want to be  
6    accused of having done something that a Chapter 7  
7    trustee would want to take a second look at.

8                   I've also been handling the  
9    litigation -- in addition to the EPA litigation,  
10   there is the BLM litigation, the Bureau of Land  
11   Management federal litigation pending in Utah and  
12   Chadbourn and Parke had been consulting on that  
13   also.

14                   THE COURT: That's the second of two  
15   types of lawsuits that Mr. Chang addressed in this  
16   lawsuit, allegedly the stealing of minerals.

17                   MR. SMOLINSKY: That's correct, your  
18   Honor, and Chadbourne has been engaged in that  
19   litigation --

20                   THE COURT: Wait. Say that again  
21   slower. Your firm has been --

22                   MR. SMOLINSKY: We have been  
23   involved in that litigation on behalf of the  
24   debtors. I have a stipulation on my disk which I  
25   was about to sign which would allow the court in

1                   Magnesium Corporation of America  
2     Utah to rule on the motion for the stay relief. We  
3     had initially opposed the judge in Utah in making a  
4     determination as to whether the stay applied to the  
5     BLM action at a hearing that I attended out in  
6     Utah. The judge was clear that she wanted to  
7     exercise her jurisdiction, which she does have  
8     jurisdiction, which coincides with your Honor's.

9                   And at that point we decided to  
10    allow the District Court to rule on the pending  
11    motions. It's a motion -- the case was dismissed  
12    and there's a motion pending by the government to  
13    reopen that case. And there is one or two other  
14    motions that the judge was prepared to rule on.

15                  THE COURT: Now, if that matter were  
16    handled on the merits, I thought I heard you saying  
17    you settle with stay type issues. Is that  
18    something that Chadbourne would be doing, or the  
19    law firm that Mr. Chang identified would be doing?

20                  MR. SMOLINSKY: There was a law firm  
21    that was representing Mag Corp prior to the  
22    petitioner date in that litigation. When the  
23    filing happened, I reviewed the lawsuit and I  
24    thought that it was fairly clear that the stay  
25    applied with respect to that action. In that

1                   Magnesium Corporation of America  
2    regard, I thought that it would be an unnecessary  
3    expenditure of the estate assets to retain trial  
4    counsel with respect to that action, even though  
5    that counsel is probably the best suited to  
6    represent the estate if the litigation goes forward  
7    because the case --

8                   THE COURT:   That's Utah, the law  
9    firm in Utah?

10                  MR. SMOLINSKY:   That's correct.  
11    Because the case was dismissed, we thought we would  
12    deal with it purely in a bankruptcy position until  
13    such time the court in Utah decided to go forward  
14    in the evidence hearing.

15                  THE COURT:   You saw, as long the  
16    stay remained, you saw no need for any further  
17    education, or if does, to get further education on  
18    the issues?

19                  MR. SMOLINSKY:   That's correct, your  
20    Honor, our involvement has been somewhat minimal.

21                  THE COURT:   All right, continue.

22                  MR. SMOLINSKY:   We have also been  
23    working on the PacificCorp matter, and we have been  
24    involved in analyzing the rate deference, although  
25    we have regulatory counsel out in Utah that we've

1                   Magnesium Corporation of America  
2    been working with. That is the status of the case,  
3    until this motion was filed.

4                   When the motion was filed, we  
5    immediately recognized that we had no desire to  
6    stop an investigation that any participant wanted  
7    to conduct. I think that's been our position  
8    throughout the case. I don't want to speak as to  
9    the merits of the avoidance actions. I do want to  
10   make one or two comments so that it does not appear  
11   that the debtors or the Creditors Committee in any  
12   way shook their responsibilities with respect to  
13   investigating a cause of action that could be worth  
14   tens of millions of dollars.

15                  The Creditors Committee did, as Mr.  
16   Top stated, conduct a preliminary investigation. I  
17   think the -- I didn't go back to check, but I noted  
18   in the reply papers of the movants, I think they  
19   said that they spent only 87 hours of legal time in  
20   analyzing the avoidance of legal actions.

21                  I think Mrs. Grubin also mentioned  
22   their contingency counsel has spent somewhat less  
23   time than that, and concluded there are viable  
24   causes of action. In addition, Willkie Farr &  
25   Gallagher conducted an investigation which the



1                   Magnesium Corporation of America  
2    debtors paid for prior to the bankruptcy case. I  
3    don't have the time records, so I can't speak as to  
4    how much Peter J. Solomon investigated the case,  
5    and their fees were substantial, although I'm not  
6    privy to the level of investigation they did.

7                   But coming out of these  
8    investigations was the understanding that in 1996,  
9    when these dividends were made, they were made as  
10   disclosed in the prospectus which was disclosed for  
11   the issuance of the bonds to the bondholders. And  
12   we presume that they made their own investigation  
13   as to the solvency of the company at that time  
14   after giving the effect of the dividends, and we  
15   believe there is a defense on the part of Renco on  
16   solvency throughout this period of time, and I  
17   think we also understand that in the metal industry  
18   there was a significant drop in prices that led to  
19   the bankruptcies of many companies in this industry  
20   in the late '90s and early 2000s.

21                  That's all I'll say on the  
22    substance, I just wanted to put that on the record,  
23    because of the inference that we have somehow sat  
24    on our hands or the committee has somehow sat on  
25    their hands with this cause of action.

1                   Magnesium Corporation of America

2                   With that said, we have in no way to  
3   try to stop an investigation. As a matter of fact,  
4   I think Mrs. Grubin has indicated that we have been  
5   in discussions with them, and I think the  
6   purchaser, with respect to the these issues, I had  
7   disbursed a commission to the Ad Hoc Committee,  
8   seeking to provide them with as much comfort as I  
9   could, that any investigation that would be  
10  conducted by the Ad Hoc Committee would give them  
11  comfort that they would not be giving up anything  
12  of substance.

13                  I spoke to the Renco Group and  
14  received their assurances that they would not raise  
15  Cybergene as a defense to any cause of action,  
16  for instance. With respect to the 108 issues, I  
17  have not had the conversation directly with Renco  
18  as to whether they would agree to the extent it's  
19  necessary, to agree to toll a period that the  
20  Chapter 7 trustee would have and an Ad Hoc  
21  Committee would not.

22                  I don't know if there would be any  
23  difference in the statute of limitations, whether  
24  it's a Court issue or whether it's a private issue.  
25  We discussed the issue in substance Wednesday

1                   Magnesium Corporation of America  
2    night, I believe at midnight, and I was at trial  
3    all day yesterday, so I have not had a chance to  
4    follow-up on that.

5                   I would know that the Ad Hoc  
6    Committee intends to use contingency counsel to  
7    bring this action. I'm not quite sure I understand  
8    why the committee can't retain the same committee  
9    in the contingency action to conduct the  
10   investigation and bring the action.

11                  Nevertheless, the stipulation I  
12   provided would provide the Ad Hoc Committee of  
13   bondholders would give the rights to pursue those  
14   actions on behalf of the United States.

15                  The only thing I wanted to -- I  
16   wanted to add on a couple other things. With  
17   respect to the administrative expenses, I guess I  
18   have a personal interest, I guess, the Creditors  
19   Committee feels conflicted not to raise their --  
20   whether they represent a group of creditors who are  
21   entitled to an investigation, but I can say that we  
22   have been proceeding down the path of anticipating  
23   that the monies in the estate would be available  
24   for distribution to administrative creditors.

25                  I think the Creditors Committee, at

1                   Magnesium Corporation of America  
2    least the counsel, had made a determination that  
3    they did not want to expend the remaining amounts  
4    and gamble them on legal fees in connection with  
5    the lawsuits on actions against affiliates. But we  
6    clearly were in the same big position. We don't  
7    want to stop the investigation, but we don't think  
8    that we necessarily should finance it.

9                   Contingency counsel, if it's fully  
10   contingent, doesn't need the money that's at this  
11   time sitting in the estate. We would ask if the  
12   court is inclined to convert the case, that at  
13   least we are able to receive as much as we can from  
14   the remaining assets of the estate in order to pay  
15   outstanding and allowed fees.

16                   In terms of the estate being  
17   administratively insolvent, I would hope the test  
18   is clear and show that the company is  
19   administratively insolvent, but think, Mrs. Grubin,  
20   if the case is successful, the estate won't be  
21   insolvent, and that's a reason for keeping the  
22   Chapter 11 open.

23                   The added expense of doing a  
24   liquidating plan versus conversion I don't think  
25   necessarily goes in favor of a Chapter 7 trustee,

1                   Magnesium Corporation of America  
2     because ultimately, while you don't have to  
3     negotiate a plan with the government, you still  
4     have to reconcile claims. And we would argue that  
5     the debtors are in the best position to reconcile  
6     those claims to make sure, if there is money, to  
7     distribute it pro rata in the proper creditor  
8     claims.

9                   THE COURT: At that last point you  
10    are not talking about Chadbourne, you are talking  
11    about your client?

12                  MR. SMOLINSKY: Yes, the officers  
13    are still working.

14                  THE COURT: You still have a  
15    skeleton crew?

16                  MR. SMOLINSKY: We have no  
17    employees. We are compensating Michael Legge, the  
18    CEO of the company; Todd Haggard, the CFO; and Lee  
19    Brown, who is the head of the administration, who  
20    have been assisting me in the winddown affairs, and  
21    presumably, if this case continues would continue  
22    to assist Chadbourne & Parke in helping with the  
23    affairs in doing whatever is necessary.

24                  THE COURT: To what extent would  
25    they be available or unavailable if we went either

1                   Magnesium Corporation of America

2   with an 11 trustee or a 7 trustee?

3                   MR. SMOLINSKY: I've not had that  
4   conversation with them. Obviously, it would be  
5   within their rights to resign from those officer  
6   positions.

7                   THE COURT: Except I think there's a  
8   duty in Chapter 7 to cooperate with the Chapter 7  
9   trustee.

10                  MR. SMOLINSKY: I would have no  
11   doubt that they would cooperate with a Chapter 7  
12   trustee the best they can.

13                  THE COURT: Okay, keep going.

14                  MR. SMOLINSKY: Your Honor noted the  
15   STN issue, and I was advised that I had not offered  
16   up that as a conclusion, and I think the record is  
17   clear that I had; and I do think it's appropriate.

18                  The 108 point, I'd like to think  
19   more about that in terms of how we get someone  
20   comfortable in an investigation that they would not  
21   lose any rights that a Chapter 7 trustee would  
22   have. Certainly, it's not the intent of the  
23   debtors to have anyone waive any rights that the  
24   Chapter 7 trustee would have; and I would endeavor  
25   to provide that, and if I were to provide that,

1                   Magnesium Corporation of America

2   then perhaps your Honor would move toward Chapter 7  
3   in order to resolve that issue.

4                   In terms of the funding that we had  
5   raised in our papers, the debtor certainly didn't  
6   intend to be heavy-handed. We simply noted in the  
7   draft papers that we were intending to file, that  
8   the funding terminated upon the appointment of a  
9   Chapter 11 trustee or Chapter 7 trustee, which  
10   every loan document that I've seen contains that  
11   proviso.

12                  And what we tried to accomplish is a  
13   funding mechanism where U.S. Mag has an economic  
14   interest in certain of the litigations and they  
15   would fund the estate, which would also allow us to  
16   conduct a winddown that would essentially reduce  
17   the administrative expenses that currently exist  
18   against the estate by dealing with the fees that  
19   have been incurred since the sale when U.S. Mag  
20   took over operations of the business, which would  
21   certainly reduce my fees. So it's somewhat  
22   self-serving, but it would also reduce the  
23   administrative expense claims that have been  
24   asserted against the remaining funds in the estate,  
25   which would be better for all other administrative

1                   Magnesium Corporation of America  
2     creditors.

3                   It would also allow us to keep open  
4     the bankruptcy case without cost for the  
5     administration of the estate while the  
6     investigation proceeds. I can't say that the  
7     funding will last forever, but to the extent -- I  
8     would anticipate that the investigation would be  
9     conducted by the Ad Hoc Committee or Creditors  
10    Committee in short order, and at that time we would  
11    know whether the grounds still exist for  
12    commencement of an action. And if it does, then  
13    that action would be commenced.

14                  We also provided in our stipulation,  
15    our STN stipulation I'll call it, to the extent the  
16    parties believe at any time in the future that they  
17    are not getting under the stipulation what a  
18    conversion to Chapter 7 or what a Chapter 11  
19    trustee would have, that they would have the right  
20    to renew their motion.

21                  MS. GRUBIN: Your Honor, I would  
22    think that these are settlement negotiations that  
23    fall within 408.

24                  THE COURT: Sustained.

25                  MR. SMOLINSKY: I apologize, your



1                   Magnesium Corporation of America

2   Honor, I didn't intend to get into the settlement  
3   discussions. I would state on the record that the  
4   debtors, in connection with any order that your  
5   Honor entered with respect to an alternative, other  
6   than conversion or the appointing of a Chapter 11  
7   trustee, that we would certainly understand that  
8   that order reserved the rights without prejudice to  
9   a party coming in and seeking to reassert the  
10   motion at any time.

11                   I apologize for getting into the  
12   settlement; was simply talking about the debtor's  
13   position with respect to make a wind down conducted  
14   and finalized.

15                   I think that's all I have on the  
16   issues, your Honor. If your Honor is inclined to  
17   convert the case because your Honor believes that  
18   we cannot afford proper investigation without a  
19   Chapter 7, I would ask for the opportunity to  
20   withdraw the debtor's objection as opposed to  
21   having it overruled. But I would like to hear your  
22   Honor's thoughts on our positions here today.

23                   THE COURT: All right. Ms. Davis, I  
24   think the spirit of what you requested a minute ago  
25   would be best served by giving Ms. Grubin a chance

1                   Magnesium Corporation of America  
2   to reply and then speak, unless you would like to  
3   waive that.

4                   MS. DAVIS:   That's fine, your  
5   Honor.   I would just ask in speaking, I'm a little  
6   ignorant to the facts here because this is a case  
7   that's one of my colleagues, Brian Masumoto, if we  
8   could have means with the respect to the fraudulent  
9   conveyance, I needed to know that number and if it  
10   can be representation to the aggregate  
11   administration expenses that are required.

12                  THE COURT:   Good, that's a good  
13   reason for you to defer for your comments till you  
14   get that information.

15                  THE COURT:   Ms. Grubin, some of that  
16   may be in your lap and some of that may be in Mr.  
17   Smolinsky's lap.

18                  MS. GRUBIN:   That's correct, your  
19   Honor.   First, while it's still fresh in our minds,  
20   we believe that there may be up to and in excess of  
21   90 million dollars --

22                  THE COURT:   90?

23                  MS. GRUBIN:   90, yes.   And in our  
24   motion, and if I might direct Ms. Davis' attention  
25   to -- bear with me, please.

1 Magnesium Corporation of America

2 THE COURT: The prospectus.

3 MS. GRUBIN: The prospectus.

4 THE COURT: I must say I missed it,  
5 just like Ms. Davis did.

6 MS. GRUBIN: I would actually direct  
7 Ms. Davis' attention to footnote 1A point 4 of our  
8 motion, which speaks about \$8.5 million of the net  
9 proceeds from the note issuance used to redeem  
10 preferred stock from the group and, additionally,  
11 46.2 million of the proceeds plus cash of 34.8  
12 million was distributed as a dividend group and to  
13 compensate certain Mag Corp executives so right  
14 there you have 89 million. And also, your Honor, I  
15 would suggest that, and it speaks about that in  
16 footnote 2, page 5, it talks about there may indeed  
17 be --

18 THE COURT: Avoid management fees?

19 MS. GRUBIN: Correct, your Honor, of  
20 100,000 dollars a month, and that dated back a  
21 number of months before the August '01 filing of  
22 the petition. And then we also understand --

23 THE COURT: The multiplier could be  
24 significant. How many months are we talking about?

25 MS. GRUBIN: Your Honor, I couldn't

1                   Magnesium Corporation of America

2    answer the court at this point. I don't think it's  
3    more than 12 prepetition, but --

4                   THE COURT: What?

5                   MS. GRUBIN: -- we could submit  
6    that subsequent to today.

7                   THE COURT: But if it is 12, and I  
8    recognize that you carefully did make  
9    representations where you didn't know, we may be  
10   talking about 12 times 100,000.

11                  MS. GRUBIN: That's correct, your  
12   Honor.

13                  THE COURT: Okay.

14                  MS. GRUBIN: And then, finally,  
15   there are also -- there is a potential cause of  
16   action for breach of fiduciary duty, and I confess  
17   not to be a bankruptcy tax expert, your Honor, but  
18   there may be some valid causes of value to tax  
19   benefits to related entities due to financial  
20   losses sustained by the debtors, because the  
21   debtors, as I understand it, reported on a  
22   consolidated basis. And the motion does speak to  
23   that sort of -- doesn't really elaborate on it too  
24   much, but that is a possible related cause of  
25   action that I couldn't put a number on at this

1                   Magnesium Corporation of America

2   point in time.

3                   THE COURT:   Okay.

4                   MS. GRUBIN:   And I think that Mr.

5   Smolinsky is more versed -- well versed in the case

6   to, perhaps, speak to the admin expenses.   But I

7   would just like to point out of these fees that are

8   unpaid in this case, my understanding is that the

9   fee orders in this case, other than with respect to

10   Willkie Farr & Gallagher, have all been interim fee

11   orders so that there have been no final allowable

12   final fee amounts in this case.

13                   I just want to make sure everyone is

14   aware of that.   Your Honor, I really will just

15   reiterate what we said in our motion and reply, but

16   I would like to respond to a few points that were

17   raised.

18                   I would point out that counsel has

19   made itself available on a contingency basis to a

20   trustee and had spent about 60 to 80 hours

21   reviewing various documents in the file of the

22   bankruptcy to determine that there were indeed

23   valid -- in their opinion, valid and viable causes

24   of action.

25                   I think Mr. Smolinsky mentioned a

1                   Magnesium Corporation of America  
2   number -- a smaller number than that; and that is  
3   in comparison to what they understood Chapman and  
4   Cutler's time of about 82 hours. I would also note  
5   that this identifies an available contingency  
6   counsel will not be available unless there is a  
7   trustee appointed in this case. And that is --

8                   THE COURT: I saw that, although  
9   only in the letter, and presumably that's because  
10   he wants the benefit of whatever 108 arguments he  
11   can make.

12                  MS. GRUBIN: That's correct, and he  
13   wants to make sure there is no underbrush of  
14   uncertainty and his firm can move forward with the  
15   substantive portions of the lawsuit. And that to  
16   us is fairly significant, because that is why we  
17   need a trustee in our opinion here, and that's why  
18   we're asking for a trustee, because while there may  
19   indeed be other counsel out there, and I understand  
20   my clients did speak to a number of other firms,  
21   there may be some time delay and perhaps even  
22   availability concerns of other contingency counsel.  
23   I would also point out that the Peter J. Solomon  
24   firm that it was -- excuse me, the FS to the  
25   committee, my understanding, and I think Mr. Top

1                   Magnesium Corporation of America  
2     can affirm this, is that they did spend a great  
3     deal of time trying to bring a buyer to the table,  
4     but they did not undertake any solvency or  
5     insolvency analysis or any of the other kinds of  
6     detailed analysis that would be necessary to  
7     preclude a cause of action, particularly fraudulent  
8     conveyance causes of action.

9                   Your Honor, I would also say that  
10    there will be -- there does not seem to be funds in  
11    the estate to fund the committee's prosecution of  
12    these causes of action for them to have completed  
13    their investigation, and it seems to me where there  
14    is identified contingency counsel who is available  
15    to investigate and prosecute and pick up the tab on  
16    these expenses, that that is something that the  
17    court should consider in reviewing whether or not  
18    to grant our motion.

19                  I would point out that whether one  
20    is hopelessly or unhopelessly administratively  
21    insolvent, one is invariably insolvent, and I would  
22    also hope that the three employees would be out in  
23    Utah, as your Honor suggested, to assist the U.S.  
24    trustee to reconcile claims administration or  
25    various litigations in this case.

1 Magnesium Corporation of America

2 One other thing I'd like to point  
3 out to the court, is that we would ask that the  
4 court rule as swiftly as possible on our motion  
5 because we are looking at, as I said before, the  
6 546(a) which is two years, and runs out this  
7 August.

8 That's all I have, your Honor,  
9 unless the court has questions.

10 THE COURT: No, I don't.

11 MS. GRUBIN: Thank you, your Honor.

12 THE COURT: All right, Mr. Top, Ms.  
13 Wallace, anything to add, to that?

14 MS. WALLACE: No, your Honor.

15 MR. TOP: Your Honor, I guess just  
16 to relate to what Ms. Grubin said relating to Peter  
17 J. Solomon; obviously they conducted financial  
18 reviews during the relevant period of time during  
19 the bankruptcy and issues of how much financing was  
20 needed and what are the assets and liabilities are  
21 for purposes of providing that information to the  
22 committee as well as making that information  
23 available to various buyers. I'm not aware of any  
24 analysis they completed to prior periods, except to  
25 the extent they looked at whatever had been



1                   Magnesium Corporation of America

2   available to Renco and Mag Corp during the prior  
3   periods.

4                   I will say, although, that they did  
5   spend some time reviewing transfers and the like,  
6   and I think we had, and we provided to the Ad Hoc  
7   group, what we thought were transfers, but to the  
8   best of my knowledge, your Honor, that's pretty  
9   much the extent of their solvency type analysis  
10   with respect to the debtors.

11                  THE COURT: Thank you, Mr. Top.

12                  Mr. Seidel, would you like to be  
13   heard?

14                  MR. SEIDEL: Yes, your Honor, just  
15   briefly. Barry Seidel from Cadwalader, Wickersham  
16   & Taft. Your Honor, I rise today only to comment  
17   with respect to the discretionary nature of the  
18   funding referred to in the debtor's papers.

19                  Just so it's clear, it was partially  
20   discretionary and partially committed. It was a  
21   500,000 dollar facility that we had offered. The  
22   initial 250,000 dollars of that was to be spent, it  
23   was committed. The balance, as of the time we  
24   negotiated that, we didn't know what was down the  
25   road in this Chapter 11 case. We didn't said we

1                   Magnesium Corporation of America  
2    wanted approval so we wouldn't have to incur the  
3    expense twice and the Renco group would be -- the  
4    agreement was subject to getting a Court order and  
5    documents in the transaction, but that was  
6    concerning discussions we had with Mr. Smolinsky  
7    six, seven months ago.

8                   THE COURT: Long before you had a  
9    motivation to bribe me.

10                  MR. SEIDEL: Your Honor, it had  
11    nothing to do with influencing the outcome here.  
12    Mr. Smolinsky has addressed the draft stipulation.  
13    I cannot tell your Honor why it wasn't filed all  
14    these months, but it hadn't been, and the reason it  
15    was negotiated at all was because of Mr.  
16    Smolinsky's concern that the estate would end up  
17    administratively insolvent.

18                  This was a financing vehicle to  
19    allow the estate to continue and wind up and this  
20    was not necessarily a situation where we would  
21    substitute the Renco Group as the unpaid advocate,  
22    because there were recognitions in there that would  
23    allow for the payment of indebtedness only from  
24    assets recovered, so we are not going to burden the  
25    estate.

1 Magnesium Corporation of America

2 THE COURT: You are not becoming a  
3 new DIP lender, that would be taken care of?

4 MR. SEIDEL: That's correct, your  
5 Honor.

6 THE COURT: Could you, please, I  
7 thought debtor's counsel was going to address that  
8 issue.

9 MR. SEIDEL: Of course, I just  
10 wanted to make sure people who wanted to be heard  
11 would have an opportunity.

12 THE COURT: Mr. Smolinsky, do you  
13 want to be heard?

14 MS. DAVIS: Your Honor, can I ask  
15 whether it was in the original DIP order there was  
16 a carveout for the Chapter 7 Trustees?

17 THE COURT: There was a DIP order  
18 and the department was paid off. It is usually my  
19 practice to require a carveout, but I don't  
20 remember whether I was doing that when this case  
21 was filed, Mr. Smolinsky, you can address that.

22 MR. SMOLINSKY: In this issue I  
23 think there was a 50,000 dollar carveout, it might  
24 have been 100,000 for a Chapter 7 trustee, but as  
25 your Honor noted, as part of the sale, the DIP

1                   Magnesium Corporation of America  
2   financing was satisfied. I don't know what the  
3   status of that carveout is.

4                   THE COURT: Okay. Go ahead with  
5   your other points.

6                   MR. SMOLINSKY: I was only going to  
7   comment on the question raised by the U.S. Trustee  
8   regarding the management fees, and it's really  
9   testing my memory, but I believe the management  
10   fees ceased at some time substantially prior to the  
11   filing. The company did not have the cash  
12   available to pay those fees. I don't remember  
13   whether it was nine months before the filing or  
14   sometime before or after that, but it's not the  
15   full 12 months within the, I guess, the preference  
16   period, if that's what you are looking at, before  
17   the year of the filing.

18                  THE COURT: Well, I'm not going to  
19   lawyer for the bondholders, but from time to time  
20   creditors have asserted that management fees of  
21   these characters are fraudulent conveyances and not  
22   just preferences.

23                  MR. SMOLINSKY: Correct. On the  
24   issue of administrative expenses, I was trying to  
25   get from Bankruptcy Services, Inc., who is our

1                   Magnesium Corporation of America  
2   claims agent, a schedule, a register of the admin  
3   claims. I didn't get it prior to leaving for Court  
4   this morning. So I can't report to you today on  
5   what the claims register looked like.

6                   I'm not aware of any claims, other  
7   than the ones that I've talked about here today.  
8   And if your Honor is inclined to put this over to  
9   see whether the financing makes sense at some  
10   future date, I could be prepared to give your Honor  
11   a full report on the status of that.

12                   In terms of the issue of whether  
13   this issue needs to be decided today, I would only  
14   note, I believe that under 546, a one year period  
15   would start upon the agreement of a Chapter 7  
16   trustee, whether it's converted today or tomorrow.  
17   As long as the conversion happens before August,  
18   there would be a one-year period, I don't think  
19   there's a tag on for the five months between now  
20   and August, and then you would add a year to that.

21                   So I think as long as the this Court  
22   orders conversion before August, I think the result  
23   is the same, the trustee would have a one-year  
24   period.

25                   I would also note that I don't know

1                   Magnesium Corporation of America  
2   whether a Chapter 11 operating trustee makes sense  
3   here. I think if we're going to change the nature  
4   of this case, I would think that for administrative  
5   costs, I think a Chapter 7 trustee would avoid the  
6   cost of an ongoing committee and receive money on  
7   quarterly fees and avoid the expense of preparing  
8   operating reports and the like, I would just note  
9   that for the record.

10                   THE COURT: What I think, and this  
11   is for the benefit of all, that when I talked about  
12   an issue as to the applicability of 108 in terms of  
13   situations of this type, I was really thinking  
14   about what you just said, Mr. Smolinsky, which is  
15   546(a)(1).

16                   In the fact of whether a debtor in  
17   possession is deemed for some purposes to be a  
18   trustee, whether that would be the first trustee  
19   appointed, and that's the conflict in the cases  
20   that I was referring to at the time I looked at it,  
21   I'm not expressing a view on the issue. But that  
22   was a matter of concern to me.

23                   MR. SMOLINSKY: And I think that's  
24   resolvable within the confines of an STN type  
25   order.

1 Magnesium Corporation of America

2 THE COURT: All right anything else,  
3 anybody, before Ms. Davis? Okay Ms. Davis.

4 MS. DAVIS: Yes, good morning, your  
5 Honor. Tracy Hope Davis, for Carolyn Schwartz, the  
6 U.S. trustee. I actually had an opportunity to  
7 review a memo my colleague, Brian Masumoto,  
8 prepared in connection with this hearing. I'm  
9 going to share some of his comments and a few of my  
10 own, based upon what the parties said today.

11 Mr. Masumoto had advised me that it  
12 was the U.S. Trustee's pictures that we didn't have  
13 an objection to the appointment of a Chapter 7  
14 trustee.

15 MR. TOP: This is brought to the --  
16 I'm having a hard time hearing.

17 MS. DAVIS: I have a follow up. As  
18 I said, I conferred with my colleague, Brian  
19 Masumoto, who is the attorney assigned to this case  
20 who understood and voiced to me that the U.S.  
21 trustee had no objection to the conversion of this  
22 case.

23 Our concern was that there might be  
24 duplication with respect to the work that had  
25 already been done by the lawyers who had commenced,

1                   Magnesium Corporation of America

2     I guess, the investigation with respect to whether  
3     there was going to be a preference or whether there  
4     were preference or avoidance actions to be pursued.  
5     It's my observation, in speaking with the parties,  
6     that while the grounds for cause to convert this  
7     case might be insolvency or issues of a conflict, I  
8     think the issue of insolvency is more important and  
9     goes toward whether the court should grant the  
10    conversion of this case.

11                   The issues of the insolvency,  
12    however, cannot be resolved, I think at this point,  
13    at this moment, and that means today. And I think  
14    the court would be assisted with the results from  
15    the bar date that has already been requested, and I  
16    believe that the date does not expire today, but it  
17    might expire early next week. Those results might  
18    be important to the court to determine whether the  
19    debtor is actually administratively insolvent or  
20    not.

21                   Based upon the comments of the  
22    parties today, the court may accept those  
23    representations as useful, but I think that a  
24    response from the debtor, perhaps in a written  
25    submission or otherwise, with respect to the amount



1                   Magnesium Corporation of America  
2   of administrative claims outstanding, would be  
3   guiding to the court and definitely would be  
4   important to the Office of the U.S. trustee.

5                   THE COURT: The one problem I have  
6   is people will put in whatever they will put in by  
7   the bar date, as you note, but why would a wild  
8   card, to the extent to Mr. Chang's folks won in  
9   Utah, if they are successful, whatever was filed by  
10   the bar date would be swamped by the liability to  
11   the United States of America. And I haven't seen  
12   what the United States filed. But I would suspect  
13   that they would have filed the administrative  
14   equivalent of what the proof of claims says, we got  
15   this thing out there and we think we are entitled  
16   to this.

17                  But, in any event, we would want the  
18   claim favor to whatever we derive.

19                  THE COURT: I'm going to invite Mr.  
20   Chang to comment when you are finished.

21                  MS. DAVIS: Sure.

22                  THE COURT: If they did that, I  
23   would hardly be surprised if they had -- we are not  
24   going to get as much information because so much is  
25   going to be determined by the folks in Utah.

1 Magnesium Corporation of America

2 MS. DAVIS: Your Honor, forgive me.

3 I'm not sure what the status of this litigation is.

4 THE COURT: I don't know if we know

5 that or not. I think Mr. Chang said matters were

6 adjudicated and he didn't hold out on that, and

7 he's the best person to speak on that.

8 MS. DAVIS: Obviously, the debtors

9 are facing administrative insolvency. Ultimately

10 an insolvent debtor calls for a Chapter 7 trustee

11 or a conversion of the case, which immediately

12 relieves that issue.

13 Your Honor, to answer a couple of

14 questions you had with respect to whether a Chapter

15 7 trustee would continue with the professionals

16 that have been retained by the debtors thus far in

17 this case, it's more than likely the Chapter 7

18 Trustees do not like to reinvent the wheel and I'm

19 sure your Honor would make a recommendation

20 immediately with respect to whether they should or

21 should not, and we would advise whoever is

22 appointed that it would be likely for them to

23 continue with whoever is on board. But at some

24 point, you have to stop the bleeding and with the

25 professionals, the Chapter 7, the United States

1                   Magnesium Corporation of America

2     trustee quarterly fees accruing, it would appear  
3     that the bleeding should stop at this point.

4                   Your Honor, I had a couple other  
5     points. As your Honor is aware, a Chapter 7  
6     trustee has the requirement to marshal assets for  
7     the benefit of all creditors, and it would appear  
8     to me, your Honor, that the continuation of these  
9     proceedings in Chapter 11 would only really inure  
10    the benefits of the economic benefits of the  
11    professionals retained thus far, and I don't really  
12    see how all creditors would benefit,  
13    notwithstanding the fact that we have the ETPSA  
14    litigation in Utah.

15                  The other point, your Honor, I  
16    believe Mr. Smolinsky made a request that your  
17    Honor, perhaps, have a hearing on final fees and  
18    allowable fees at this point. Typically, in many  
19    cases, as your Honor is aware, the court will make  
20    a final ruling on professional fees before the  
21    court converts the case. I don't really know if  
22    that is that's appropriate at this time.

23                  I don't know whether there's been a  
24    finding of any wrongdoing by counsel or not, but  
25    perhaps, again, if the case is converted, a Chapter

1                   Magnesium Corporation of America  
2    7 trustee can get his arms around all the  
3    administrative fees that are outstanding.

4                   And, let me think of what else, I  
5    echo the response of Ms. Grubin, in that any  
6    officers or directors that are working currently  
7    with the debtor would have an obligation to do the  
8    same thing with a Chapter 7 trustee. That's it. I  
9    hope my comments have been helpful to your Honor.

10                  THE COURT: Yes, they have, thank  
11    you.

12                  MS. DAVIS: Thank you.

13                  THE COURT: Mr. Chang, were my  
14    adoptions correct or incorrect?

15                  MR. CHANG: Don't worry.

16                  THE COURT: Don't worry about being  
17    diplomatic.

18                  MR. CHANG: It is correct. We  
19    intend to file an administrative claim with the EPA  
20    lawsuit, and the government may also file a claim  
21    of reclamation with a claim previously leased by  
22    Mag Corp. On the issues that was what raised was  
23    the states of what I regard as the regular lawsuit,  
24    the EPA lawsuit, as I stated in the letter, there  
25    are motions for summary judgment, and we have no

1                   Magnesium Corporation of America  
2   way of knowing whether they would be ruled on, and  
3   even if they were ruled on, I don't think it will  
4   dispose of the case entirely, but certainly it may  
5   go a long way to settling if there is a great deal  
6   of uncertainty even if there were a decision on the  
7   motions.

8                   THE COURT: Thank you.

9                   MS. DAVIS: Excuse me, your Honor.  
10   I have one problem. I have a conference on  
11   Adelphia, I was supposed to be on at 11, I need to  
12   call my office.

13                  THE COURT: You are excused for that  
14   purpose, and I will tell you what I'm going to do  
15   is I'll take a recess to about quarter of 11 and  
16   then I'm going to give you at least some thoughts.  
17   And so we're in recess until 11:15.

18                  (Recess taken.)

19                  MS. GRUBIN: Thank you, Judge.

20                  MR. TOP: Your Honor, we'll keep the  
21   line open.

22                  THE COURT: I would recommend that.

23                  (Recess taken.)

24                  THE COURT: Have a seat. At the  
25   outset I want to talk about what this case is not.

1                   Magnesium Corporation of America

2   This case is not, at least on the record presented  
3   to me so far, a case about fraud or mismanagement  
4   about an incumbent debtor or its counsel. It's not  
5   a Hampton Hotel case, where a year or two ago I  
6   granted a motion by the U.S. trustee to convert a  
7   case based on the misconduct of the debtor in  
8   possession. It's not even, in my view, a bleeding  
9   case where I think that since the time of the sale  
10  the debtor has been very conscientious in trying to  
11  keep costs under control.

12                   What is more important, in my view,  
13  is the inherent conflict that needs to be addressed  
14  by one means or another to insure that the claims,  
15  if any, and I underscored the if any, that  
16  bondholders or creditors might generally have, are  
17  properly investigated and prosecuted.

18                   And the uncertainty with respect to  
19  administrative claims, and the potential, not the  
20  certainty, the potential that the United States or  
21  the EPA do prevail in Utah and have administrative  
22  claims that could swamp the others.

23                   In other words, this case, if  
24  anything, is much more like the PSINet Consulting  
25  case, where there was no indication that the

1                   Magnesium Corporation of America  
2   management of PSINet had improperly captained the  
3   PSINet Consulting's ship, but the company claims  
4   were such that the thought a trustee was required  
5   to insure that any identifiable claims against the  
6   corporate parent or the other entities in the  
7   corporate family could be properly addressed.

8                   I usually prefer STN or Commodore  
9   orders to deal with conflicts of that character. I  
10   think that more precisely, and in a less  
11   heavy-handed way, deal with the concerns that need  
12   to be addressed. Here, however, I have unique  
13   needs. I have the need not to foreclose creditors  
14   from making a 108 argument or a 546(a)(1)(b)  
15   argument, although I don't want to pre-judge that  
16   in any way.

17                   And, frankly, and I want to try to  
18   say this as antiseptically as I can, I prefer,  
19   frankly, to have an independent trustee consider  
20   whether or not to bring claims against the debtor's  
21   affiliates or others, rather than the movants, or  
22   at least in terms of having the movant's captaining  
23   the ship, where some of the claims that they might  
24   wish to assert, although they should certainly have  
25   the right to assert them, because they go back so

1                   Magnesium Corporation of America

2   far and/or because they relate to a debatable issue  
3   of insolvency, are not by any means slam-dunks.

4                   My discretion in that regard is  
5   formed in part by the fact that the two counsel for  
6   the Creditors Committee, Willkie Farr and  
7   Gallagher, Chapman and Cutler, both are very  
8   capable law firms. The matters of the dividends  
9   and even the management fees are matters that were  
10  of public record for a long, long time.

11                  And the fact that they did not feel  
12  compelled immediately to take action causes me to  
13  wonder whether the claims -- again, I'm certainly  
14  not pre-judging them -- are not necessarily the  
15  slam-dunks that somebody might perceive that they  
16  are and the amount potentially to be recovered is  
17  very large, any equation that takes into account  
18  the likelihood of recovery also must take into  
19  account the likelihood of success, which is  
20  something that I'm not in a position to pre-judge.

21                  With all of those things said,  
22  subject to what I'm going to say in a minute, I  
23  believe that we are going to need, and I say this  
24  reluctantly because I think the debtor's counsel  
25  has done a very good job in this case and has tried



1                   Magnesium Corporation of America

2    very hard to maximize value, has tried very hard to  
3    get value, other than a deal with what turned out  
4    to be an affiliate.

5                   We are going to need an independent  
6    captain of the ship. And I don't believe that an  
7    STN Commodore order, notwithstanding my usual  
8    predilection for entering them, would skin the cat  
9    here.

10                  My judgment in this regard is also  
11    informed by the fact that the two main battles that  
12    would be fought, if the estate had to fight them  
13    one with the EPA and the United States government  
14    and the other with PacificCorp, would be handled by  
15    Utah counsel or regulatory counsel, respectively,  
16    rather than Chadbourne in any material respect.  
17    And, therefore, I would not have the usual need to  
18    get the benefit or utilize the benefit of  
19    Chadbourne's learning. And if I or a trustee were  
20    to conclude otherwise, I think we all agree that  
21    Chadbourne could continued to serve under 237(e)  
22    for a limited purpose to accomplish those goals, if  
23    needed.

24                  I must say, by the way, that with  
25    respect to any claims that might be asserted,

1                   Magnesium Corporation of America  
2   because of my uncertainties, again without  
3   pre-judging, as to their ultimate strength and  
4   because of the liquidity condition of this estate,  
5   I almost certainly will not approve any legal fees  
6   for either litigating or even investigating those  
7   claims, unless they are on a contingent fee basis.  
8   Therefore, I believe that I need independent and  
9   objective review and management of this case with a  
10   trustee, which in the first instance could be  
11   either under 11 or 7.

12                   I believe that the grounds for both  
13   are shown, although I think my earlier comments  
14   made clear that we are not talking about an (a)(1)  
15   to mismanagement, we are solely talking about  
16   what's in the interest of creditors. And I think  
17   that the discretion, including but not limited to,  
18   that I have vis-a-vis conversion, and  
19   uncertainties, even though I have no knowledge as  
20   to the possibility of the administrative  
21   insolvency, provide like basis under 1112.

22                   I am very mindful of the ways by  
23   which the Chadbourne firm has acted responsibly up  
24   to this date and has continued to act responsibly,  
25   even through this argument, and what Mr. Smolinsky

1                   Magnesium Corporation of America  
2    said about wanting to be given an opportunity to  
3    consider whether he would withdraw this opposition.  
4    I'm going to give you a week to decide that, Mr.  
5    Smolinsky.

6                   Likewise, I'm going to give you that  
7    same week to caucus with Ms. Grubin and Mr. Top and  
8    the U.S. trustee, and if the Indentured trustee  
9    wants to be heard, I'm not even going to keep the  
10   Indentured trustee out of that discussion, to  
11   consider whether 11 is superior to 7, although I  
12   must say that my inclination is to say that the 7  
13   is the more appropriate vehicle under these  
14   circumstances.

15                  If there is a consensus or agreement  
16   that an 11 trustee more appropriately addresses the  
17   needs of creditors, than is the 7 trustee, I would  
18   not be of a mind to veto that. In the inability to  
19   agree, I think I would more likely come out with  
20   the view that the 7 trustee is more appropriate.

21                  I see that Mr. Zipes has come in and  
22   is now representing the interests of the U.S.  
23   Trustee, rather than Ms. Davis.

24                  Mr. Zipes, I know the U.S. trustee  
25   has a normal preference under circumstances like

1                   Magnesium Corporation of America  
2    this when a judge believes that a Chapter 7  
3    conversion is ultimately going to be appropriate or  
4    judges act without delay here; however,  
5    notwithstanding that preference which I share, this  
6    is not a case of fraud or mismanagement, this is  
7    not a case of bleeding, this is not a case of a  
8    fire that needs to be put out within the next  
9    couple of days. I would rather permit the  
10   thoughtful efforts by the parties in interest to  
11   arrange a smooth conversion, and that risks that  
12   one sometimes encounters, like in a Hampton Hotel  
13   situation, where immediate conversion is  
14   appropriate, are not my view presently here.

15                   This is not a case of a corrupt  
16   debtor, it is a case where the debtor, no matter  
17   how hard it tries, has certain realities with which  
18   it has to confront itself.

19                   Not by way of reargument, but I will  
20   take questions. Obviously, what is contemplated in  
21   this is I need Mr. Smolinsky to caucus with his  
22   folks and to give thought to what he wants his  
23   position to be, and to caucus with Ms. Grubin about  
24   implementing mechanics.

25                   In the event of a failure to agree,

1                   Magnesium Corporation of America

2     I will arrange at your option, either a conference  
3     call for or a hearing to perceive how we proceed  
4     next. But everybody here is a responsible lawyer,  
5     and I think that we can probably achieve much of  
6     this by consensus.

7                   Mr. Smolinsky, are you about to  
8     rise?

9                   MR. SMOLINSKY: Yes, sir. I do have  
10    one question that would help us. We'll obviously  
11    undertake to have those conversations with all  
12    parties.

13                  The one question I have that would  
14    provide us guidance, you had mentioned that you  
15    were uncomfortable putting the Ad Hoc Committee in  
16    the place of the examiner, per se, to investigate  
17    the matter.

18                  THE COURT: I didn't use the word  
19    examiner, I think we are talking about a trustee.

20                  MR. SMOLINSKY: Yes, one of the  
21    differences between a Chapter 11 trustee and a  
22    Chapter 7 trustee, in the Chapter 11 Trustee, it  
23    would be your Honor's determination as to who the  
24    trustee would be, I believe --

25                  MR. ZIPES: That's not right.

1 Magnesium Corporation of America

2 MR. SMOLINSKY: It's not?

3 THE COURT: No. My understanding is  
4 I will decide there will be a Chapter 7 trustee,  
5 and then that the U.S. Trustee's Office appoints  
6 one of a consulting parties in interest, but I'm  
7 certainly going to give Mr. Zipes an interest and  
8 I'm, hopefully, if you would be yielding to Mr.  
9 Zipes, which might be better to yours or mine.

10 MR. SMOLINSKY: I would just like  
11 to point out that in a Chapter 7, you would have a  
12 panel appointed and the creditors would be able to  
13 elect their own trustee. And that may be a  
14 consideration in our discussions with regard to how  
15 we fashion an order that would fulfill your Honor's  
16 issue that you are looking for someone who is truly  
17 independent.

18 THE COURT: Mr. Zipes, would you  
19 like to comment? I know this puts you into the  
20 middle of something without a whole lot of  
21 preparation.

22 MR. ZIPES: This is the Achaian of  
23 1210, 1107 and 1104. Your understanding is correct  
24 and Mr. Smolinsky's is correct as well. In a  
25 Chapter 11 situation, we would appoint a panel

1                   Magnesium Corporation of America  
2   under 701 and there would be a creditors meeting,  
3   at which point there would be an election with the  
4   creditors, so if the creditors had the votes, they  
5   would vote to appoint a trustee. In a Chapter 11  
6   situation, I've never seen that occur where there's  
7   an election, and I don't believe it's the same  
8   statute, although I'm just speculating. I believe  
9   1104 we would just appoint the Chapter 11 trustee.

10                   THE COURT: Those facts would  
11   influence by judgement.

12                   MR. ZIPES: I'm more confident with  
13   an 11 than a 7.

14                   THE COURT: I really would like  
15   independence in this investigation. All right, I  
16   don't know, though, that that goes to the level of  
17   a ruling. If that can't be consensually resolved,  
18   I know that the 11 trustee was the Ad Hoc  
19   Committee's first request. If you guys can't  
20   resolve that consensually, then I will deal with it  
21   in about a week's time.

22                   Anything else, anybody?

23                   Okay, thank you. We're adjourned.

24                   I want to apologize to the people  
25   who have been waiting for the subsequent matters on

1 Magnesium Corporation of America

2 the calendar.

3 MR. SMOLINSKY: Thank you very

4 much, your Honor

5 MR. TOP: Thank you, your Honor.

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C E R T I F I C A T E

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STATE OF NEW YORK }

ss.:

4

COUNTY OF WESTCHESTER )

5

I, Denise Nowak, a Shorthand Reporter  
and Notary Public within and for the State  
of New York, do hereby certify:

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11

That I reported the proceedings in  
the within entitled matter, and that the  
within transcript is a true record of such  
proceedings.

12

13

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I further certify that I am not  
related, by blood or marriage, to any of the  
parties in this matter and that I am in no  
way interested in the outcome of this  
matter.

17

18

19

IN WITNESS WHEREOF, I have hereunto  
set my hand this 21 day of February,  
2003.

20

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25

Denise Nowak  
DENISE NOWAK

## Miscellaneous:

01-14312-reg Magnesium Corporation of America

### Notice of Electronic Filing

The following transaction was received from entered on 2/26/2003 at 9:00 AM and filed on 2/24/2003

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